

# ASSEMBLY, No. 1720

## STATE OF NEW JERSEY 217th LEGISLATURE

PRE-FILED FOR INTRODUCTION IN THE 2016 SESSION

**Sponsored by:**

**Assemblyman RONALD S. DANCER**

**District 12 (Burlington, Middlesex, Monmouth and Ocean)**

**SYNOPSIS**

Updates corporation business tax reporting, reduces tax sheltering, and improves tax enforcement by requiring related corporations to file combined tax return using “water’s edge” approach.

**CURRENT VERSION OF TEXT**

Introduced Pending Technical Review by Legislative Counsel.



A1720 DANCER

1 AN ACT requiring “water’s edge” combined reporting approach for  
2 corporation business taxpayers, amending P.L.1945, c.162.

3

4 **BE IT ENACTED** by the Senate and General Assembly of the State  
5 of New Jersey:

6

7 1. Section 10 of P.L.1945, c.162 (C.54:10A-10) is amended to  
8 read as follows:

9 10. a. Whenever it shall appear to the director that any taxpayer  
10 fails to maintain its records in accordance with sound accounting  
11 principles or conducts its business or maintains its records in such  
12 manner as either directly or indirectly to distort its true entire net  
13 income or its true entire net worth under this act or the proportion  
14 thereof properly allocable to this State, or whenever any taxpayer  
15 maintains a place of business outside this State, or whenever any  
16 agreement, understanding or arrangement exists between a taxpayer  
17 and any other corporation or any person or firm, for the purpose of  
18 evading tax under this act, or whereby the activity, business,  
19 receipts, expenses, assets, liabilities, income or net worth of the  
20 taxpayer are improperly or inaccurately reflected, the director is  
21 authorized and empowered, in the director's discretion and in such  
22 manner as the director may determine, to adjust and redetermine  
23 such items, and to adjust items of gross receipts, tangible or  
24 intangible property and payrolls within and without the State and  
25 the allocation of entire net income or entire net worth or to make  
26 any other adjustments in any tax report or tax returns as may be  
27 necessary to make a fair and reasonable determination of the  
28 amount of tax payable under this act.

29 b. Where (1) any taxpayer conducts its activity or business  
30 under any agreement, arrangement or understanding in such manner  
31 as either directly or indirectly to benefit its members or  
32 stockholders, or any of them, or any person or persons directly or  
33 indirectly interested in such activity or business, by entering into  
34 any transaction at more or less than a fair price which, but for such  
35 agreement, arrangement or understanding, might have been paid or  
36 received therefor, or (2) any taxpayer, a substantial portion of  
37 whose capital stock is owned either directly or indirectly by or  
38 through another corporation, enters into any transaction with such  
39 other corporation on such terms as to create an improper loss or net  
40 income, the director may include in the entire net income of the  
41 taxpayer the fair profits which, but for such agreement, arrangement  
42 or understanding, the taxpayer might have derived from such  
43 transaction. The director may require any person or corporation to  
44 submit such information under oath or affirmation, or to permit  
45 such examination of its books, papers and documents, as may be

**EXPLANATION – Matter enclosed in bold-faced brackets [thus] in the above bill is not enacted and is intended to be omitted in the law.**

**Matter underlined thus is new matter.**

1 necessary to enable the director to determine the existence, nature  
2 or extent of an agreement, understanding or arrangement to which  
3 this section relates, whether or not such person or corporation is  
4 subject to the tax imposed by this act.

5 c. The entire net income of a taxpayer exercising its franchise  
6 in this State that is a member of an affiliated group or a controlled  
7 group pursuant to section 1504 or 1563 of the federal Internal  
8 Revenue Code of 1986, 26 U.S.C. s.1504 or 1563, shall be  
9 determined by eliminating all payments to, or charges by, other  
10 members of the affiliated or controlled group in excess of fair  
11 compensation in all inter-group transactions of any kind.  
12 **【Notwithstanding the elimination of all inter-group transactions in**  
13 **excess of fair compensation, if the taxpayer cannot demonstrate by**  
14 **clear and convincing evidence that a report by a taxpayer discloses**  
15 **the true earnings of the taxpayer on its business carried on in this**  
16 **State,】**

17 If a corporation is subject to the tax imposed pursuant to section  
18 5 of P.L.1945, c.162 (C.54:10A-5), then the director **【may, at the**  
19 **director's discretion,】** shall require the taxpayer to file a  
20 **【consolidated】** combined return of the entire operations of the  
21 **【affiliated group or controlled】** combined group, including its own  
22 operations and income to the extent permitted under the  
23 Constitution and statutes of the United States. The director shall  
24 determine the true amount of entire net income earned by the  
25 taxpayer in this State. The **【consolidated】** combined entire net  
26 income of the taxpayer and of the other members of its **【affiliated**  
27 **group or controlled】** combined group shall be allocated to this State  
28 by use of the applicable allocation formula that the director requires  
29 pursuant to P.L.1945, c.162 (C.54A:10A-1 et seq.) be used by the  
30 taxpayer. The return shall include in the allocation formula the  
31 **【property, payrolls, and】** sales of all corporations for which the  
32 return is made. The director may require a **【consolidated】**  
33 combined return under this section without regard to whether the  
34 other members of the **【affiliated or controlled】** combined group,  
35 other than the taxpayer, are or are not exercising their franchises in  
36 this State.

37 **【A consolidated return required by this section shall be filed**  
38 **within 60 days after it is demanded, subject to the penalties of the**  
39 **State Uniform Tax Procedure Law, R.S.54:48-1 et seq.】**

40 The member of **【an affiliated group or】** a **【controlled】** combined  
41 group shall incorporate in its return required under this section  
42 information needed to determine under this section its taxable entire  
43 net income, and shall furnish any additional information the director  
44 requires, subject to the penalties of the State Uniform Tax  
45 Procedure Law, R.S.54:48-1 et seq. **【A taxpayer shall furnish any**  
46 **additional information requested within 30 days after it is**

1 demanded, subject to the penalties of the State Uniform Tax  
2 Procedure Law, R.S.54:48-1 et seq.】

3 d. For the purposes of this section:

4 “Combined group” means the members of the group of entities  
5 that have common ownership and are engaged in a unitary business,  
6 and are subject to the tax imposed pursuant to section 5 of  
7 P.L.1945, c.162 (C.54:10A-5), or, if not subject to the tax imposed  
8 pursuant to section 5 of P.L.1945, c.162 (C.54:10A-5), meet one or  
9 more of the following:

10 (1) a member incorporated in the United States, or formed under  
11 the laws of the United States, any state, the District of Columbia, or  
12 a territory or possession of the United States, unless 80 percent or  
13 more of the member’s sales during the privilege period are assigned  
14 outside of the United States and any territory or possession of the  
15 United States;

16 (2) a member wherever incorporated or formed, if more than 20  
17 percent of the member’s sales during the privilege period are  
18 assigned to the United States or any territory or possession of the  
19 United States; or

20 (3) a member that is incorporated in a jurisdiction that is  
21 determined by the director to be a tax haven, unless it is proven to  
22 the satisfaction of the director that the member is incorporated in a  
23 tax haven for a non-tax business purpose.

24 “Common ownership” means that not less than 50 percent of the  
25 voting control of each member of a combined group is directly or  
26 indirectly owned by a common owner or owners, either corporate or  
27 noncorporate, whether or not the owner or owners are members of  
28 the combined group. Whether voting control is indirectly owned  
29 shall be determined pursuant to section 318 of the federal Internal  
30 Revenue Code (26 U.S.C. s.318).

31 (cf: P.L.2002, c.40, s.10)

32  
33 2. This act shall take effect immediately and apply to privilege  
34 periods ending after its date of enactment.

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STATEMENT

39 This bill updates the corporation business tax reporting system to  
40 reduce tax sheltering and improve the efficiency of corporate tax  
41 code enforcement. It requires related corporations to file a  
42 combined tax return using an income reporting system that is  
43 similar to those currently in place in a majority of states.

44 Most large businesses are structured as a family of corporations  
45 under common ownership and control. This type of structure  
46 facilitates the sheltering of corporate income from taxation through  
47 transactions among various related corporate entities.

1       This bill improves tax fairness by eliminating opportunities for  
2 corporate tax avoidance strategies. The bill adopts a combined  
3 reporting system that effectively treats a group of interrelated  
4 companies as a single corporation for state corporation business tax  
5 purposes, thereby reducing or eliminating the use of inter-corporate  
6 transactions to shelter income from taxation.

7       The bill is structured to avoid constitutional issues that may arise  
8 from other forms of combined reporting by instead following the  
9 widely-used “water’s edge” approach, omitting from the combined  
10 return corporations that do not independently conduct activity in  
11 New Jersey and that do very little business in the United  
12 States. However, the bill requires the combined tax return to  
13 include a related company that is incorporated in a tax haven  
14 jurisdiction. Such a company may be excluded from the combined  
15 return only if it is proven, to the satisfaction of the Director of the  
16 Division of Taxation, that incorporation in that jurisdiction was for  
17 a non-tax business purpose.

18       Combined reporting is the next generation corporate income tax  
19 compliance technique, and is presently in use by 28 states.